DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 01-0088
Sales and Use Tax
For the Years 1998-1999

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ISSUE

I. Sales and Use Tax- Manufacturing Exemption

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-3-2 (a), IC 6-2.5-5-3, 45 IAC 2.2-5-10 (c), 45 IAC 2.2-5-8 (k), *Gross Income Tax Division v. National Bank and Trust Co.,* 79 N.E. 2d 651 (Ind. 1948). *Indiana Department of Revenue v. Cave Stone*, 457 N.E. 2d 520*,* (Ind. 1983), *Indiana Department of Natural Resources v. United Minerals, Inc.,* 686 N.E.2d 851, 857, (Ind. Ct., App. 1st Dist. 1997), *Accord, Hartford Acc. & Indem. Company v. Dana Corporation,* 690 N.E.2d 285, (Ind. Ct. App. 2d Dist. 1997).

The taxpayer protests the imposition of use tax on certain equipment.

II. Sales and Use Tax-Public Transportation Exemption

Authority: IC 6-2.5-3-2, IC 6-2.5-5-27, National Serv-All, Inc. v. Indiana Department of State Revenue*,* 644 N.E. 2d 960 (Ind. Tax 1994), Indiana Waste Systems of Indiana, Inc. v. Indiana Department of State Revenue, 644 N.E. 2d 960 (Ind. Tax 1994), Panhandle Eastern Pipeline Company and Trunkline Gas Company v. Indiana Department of State Revenue*,* 741 N.E.2d 816 (Ind. Tax 2001).

The taxpayer protests the assessment of tax on certain trucks, a trailer, and parts.

III. Tax Administration- Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b)
The taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

The taxpayer is a manufacturer of ready-mix concrete for sale to retail customers. It manufactures concrete in its batch plant, and then delivers it to customers in trucks specially designed for the mixing and delivery of concrete. After an audit, the Indiana Department of

Revenue, hereinafter referred to as the "department," assessed additional sales and use tax, interest, and penalty. The taxpayer protested the assessment of tax on the Bob Cat Dozer, Kawasaki Loader, hydraulic excavator, several trucks, a trailer, related parts and the penalty. A hearing was held.

I. Sales and Use Tax- Manufacturing Exemption

DISCUSSION

IC 6-8.1-5-1 (b) provides that all departmental tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect.

Pursuant to IC 6-2.5-3-2 (a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana when the sales tax was not paid. A number of exemptions are available from use tax, including those collectively referred to as the manufacturing exemptions. All exemptions must be strictly construed against the party claiming the exemption. *Gross Income Tax Division v. National Bank and Trust Co.,* 79 N.E. 2d 651 (Ind. 1948). IC 6-2.5-5-3 provides for the exemption of "manufacturing machinery, tools and equipment which is to be directly used by the purchaser in the direct production, manufacture, fabrication . . . of tangible personal property." In *Indiana Department of Revenue v. Cave Stone*, 457 N.E. 2d 520*,* (Ind. 1983) the Indiana Supreme Court found that a piece of equipment qualifies for the manufacturing exemption if it is essential and integral to the production process. 45 IAC 2.2-5-10 (c) further describes manufacturing machinery and tools as exempt if they have an immediate effect on the property in production. The manufacturing process starts when there is a change ". . . in a form, composition, or character different from that in which it was acquired." Pursuant to 45 IAC 2.2-5-8 (k), the use of the machinery and the time of its use then determines whether or not it qualifies for exemption.

In the taxpayer's operation, the raw materials, including cement, sand, aggregate and gravel, water and other chemicals, are delivered by vendors to the taxpayer's site by various means. Aggregate, sand, and gravel are all stored in piles near the batch plant.

The Kawasaki loader and hydraulic excavator pick up the aggregate, sand, and gravel off the ground and "charge" or load the bin of the cement batch plant. These pieces of equipment are necessary for loading the initial bin of the plant since the materials are stored approximately ten to fifteen feet above ground level. Often, some of the material being added to the bins spills on the ground around the batch plant. The taxpayer then uses the smaller Bob Cat Dozer to pick up the spilled material and return it to the batch plant bin. Once the initial bin of the batch plant has been charged, the materials are transported upwards from that bin onto a conveyor belt and transported to a second bin, which measures the correct quantities of each material for a particular batch of concrete. The proportions for each component material change with weather conditions, temperature, and the desired properties of the finished concrete.

The taxpayer protests the department's assessment of use tax on the Kawasaki Loader, the Bob Cat Dozer, and hydraulic excavator. The taxpayer contends that the charging of the bins by the use of the loaders, excavator, and dozer constitutes the first operation in a series of operations that collectively comprise the integrated production process for the manufacture of its product, concrete. The taxpayer argues that the charging process is an integral part of the production process, and that the equipment used in that process should be exempt from the use tax as

machinery directly used in the direct production. The taxpayer bases its argument on the Indiana Tax Court's holding in an unpublished decision concerning a similar industry. That case is not valid authority for the proposition that the taxpayer's equipment is exempt from the use tax. The case cited by the taxpayer is a trial court judgment from which no appeal was taken. Although the Indiana Supreme Court has not ruled on the question, a majority of the panels of the Indiana Court of Appeals have held that a cited unpublished judgment has no effect as precedent. "[A] conclusion of law by a circuit court in a case from which no appeal has been taken is not binding precedent. . ." *Indiana Department of Natural Resources v. United Minerals, Inc.,* 686 N.E.2d 851, 857, (Ind. Ct., App. 1st Dist. 1997). *Accord, Hartford Acc. & Indem. Company v. Dana Corporation.,* 690 N.E.2d 285, (Ind. Ct. App. 2d Dist. 1997).

The taxpayer's production process begins when the computer measures and blends the taxpayer's various ingredients for the formulation of cement. Any equipment used prior to this time in the production process is pre-production equipment. Since the Kawasaki Loader, Bob Cat Dozer, and hydraulic excavator are used prior to the computer measurement and blending of the ingredients, these items are pre-production equipment and do not qualify for exemption from the sales and use tax.

FINDING

The taxpayer's protest is denied.

II. Sales and Use Tax-Public Transportation Exemption

DISCUSSION

Pursuant to IC 6-2.5-3-2 (a), the department assessed use tax on the taxpayer's purchase and use of several trucks, a trailer, and replacement parts. These items are used to haul aggregate for the taxpayer and others. The taxpayer protests this assessment contending that the items qualify for the public transportation exemption pursuant to the following provisions of IC 6-2.5-5-27:

> Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

The Indiana Tax Court has addressed the issue of public transportation in several cases. The first two cases involved contract hauling of garbage. In National Serv-All, Inc. v. Indiana Department of State Revenue, 644 N.E. 2d 960 (Ind. Tax 1994), the Court stated that although National Serv-All "engaged in 'public transportation' when it hauled Contract garbage," nonetheless National Serv-All did not prove "that its hauling of Contract garbage was the *predominant share* of its use of the items at issue." Id. At 959. (Emphasis in the original). The Court concluded: "Although National engaged in the public transportation of property within the meaning of IC 6-2.5-5-27 when it hauled Contract garbage, it did not prove it predominantly engaged in public transportation." Id. at 960.

The Court faced a similar issue concerning the applicability of the public transportation exemption to the contract hauling of garbage in Indiana Waste Systems of Indiana, Inc. v.

Indiana Department of State Revenue, 644 N.E. 2d 960 (Ind. Tax 1994). In that case the Court held as follows:

> Waste Management's maximum annual revenue from public transportation was 17.7 percent of its total revenue, and therefore, the remaining 80 percent of its revenue came from non-public transportation. The predominant use of Waste Management's trucks and other items, therefore, is not exempt. . .

Id. at 962.

The third case dealing with this issue in Panhandle Eastern Pipeline Company and Trunkline Gas Company v. Indiana Department of State Revenue, 741 N.E.2d 816 (Ind. Tax 2001). The petitioners were pipeline companies that transported natural gas belonging to third parties and natural gas belonging to the petitioners. In each case, the predominate use of the pipelines was to transport natural gas belonging to others. The Court, after noting the relevance of its two previous cases on public transportation, stated the following.

> If a taxpayer acquires tangible personal property for predominate use in providing public transportation for third parties, then it is entitled to the exemption. If a taxpayer is not predominately engaged in transporting the property of another, it is not entitled to the exemption.

Id. at 819.

The Indiana Tax Court has set out a two-pronged test to determine if a particular business qualifies for the public transportation exemption from sales and use tax. First the taxpayer must be predominately engaged in public transportation of the property of another. Secondly, the taxpayer's property must be predominately used for providing public transportation.

The first prong looks at the taxpayer itself. A determination must be made whether or not the taxpayer is engaged in public transportation. The second prong looks at the individual units to determine how they are used. Both prongs must be satisfied for the taxpayer to qualify for the public transportation exemption.

In this situation, the taxpayer is primarily engaged in the production of concrete. It is not predominately engaged in public transportation. Therefore, having failed the first prong of the test, the taxpayer does not qualify for the public transportation exemption from the sales and use tax for any of the years of the audit.

FINDING

The taxpayer's protest is denied.

III. Tax Administration-Negligence Penalty

DISCUSSION

The taxpayer also protested the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The taxpayer did not self assess or remit any use tax during the audit period. This disregard of the taxpayer's statutory duty constitutes negligence. The penalty was properly imposed.

FINDING

The taxpayer's protest is denied.

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